



## Evaluating Economic Policy Instruments for Sustainable Water Management in Europe

# EPIs & Water Governance

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## EPI-Water 2(1)

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# Who am I to say?

## Rhino and Couchsurfing

- Trust and rule of law (institutions, TCs)
- Development economics, 90 countries

## Smith on prosperity from size of the market

- Markets grow on trust and ideas
- Trusting carpetbaggers with ideas or Not Invented Here?
- Rice subsidies: «Why do you want to hurt my family?»
- Visible losers and invisible winners

## The line between crime and politics of redistribution?

- Governance (corruption, community, politics)
- Restructuring from failure to reform in the face of change

**Many ways to convey ideas (force, beer, jokes, bluntness),  
but we need to agree to target group sustainability.**



# From institutions to incentives to outcomes

The water sector exists in an extreme corner where...

- Political rules dominate
- Monopolies deliver «goods»
- Goods have significant externalities
- Actors are in multilateral relationships
- Information is scarce

**Governance explains the difference between success and failure in general -- and with respect to EPIs**

## Why do we care?

We are seeing increasing scarcity for clean, fresh water.

The «shadow value» of missing water is rising far above nominal prices.

Further, the effects of climate change, arriving via changes in the magnitude and frequency of water flows, will complicate our lives.

**These impacts can be reduced or reversed with changes in institutions, and EPIs can play a significant role.**

The State manages the people's water.

Social welfare maximization is possible, but so is capture by special interests (corruption) or mismanagement by ideology.

Examples:

- Saudi princes get cheap water
- Frozen rights on the Colorado River
- Land and water grabs

# Monopolies

Water requires expensive, fixed infrastructure to move.

Water sources are often shared.

Monopolies can maximize social welfare but they can also be lazy or pursue «traditional» goals.

Examples:

- You get *this* service at *this* price when we want
- We decide your water quality
- Business customers will pay more because *they* have money

# Externalities

Water use in one place affects users in other places.

It's possible to «internalize the externalities» with appropriate rights, laws and information, but those factors are expensive and perhaps overlooked.

Examples:

- Groundwater overpumping in Spain, India, California
- Water pollution in the Baltic and Netherlands
- Competition between hydropower and fish

## Multiple actors

Politicians tell regulators to direct monopolies to deliver water services that customers value

It's difficult to consider others' needs, even assuming you want to do so and especially when customers have different needs.

Examples:

- Small farmers and big farmers
- Drinking vs toilet water quality
- Rich vs poor

## Information

The value of water varies by person, use, time and place

The interdependencies of water uses are everywhere

We don't know if we will have too little or too much water tomorrow

Economics: *competitive* actors ration *private* goods at transparent *prices* from *sellers to buyers*

Politics: *authorized* representatives allocate *collective* goods of varying subjective values to the group

**Use EPIs when you *can* replace political with economical, but remember that good policies consider local institutions. ....so how does this happen?**



## Ideas can change institutions, incentives and outcomes

Many water uses have a political/social component, but many do not. EPIs clarify costs and benefits by pricing water, pollutants, etc. in a transparent way.

EPI-Water has spent the past year understanding how EPIs succeed and fail. Institutions and transaction costs end up having a significant impact on implementation and the economic, environmental and distributional outcomes.

**First step: Understand what's gone right and wrong.**

**Second step: Change your ideas about water management.**

**Third step: Point those ideas at institutions. For example...**



## Some of my examples

Private water uses can be allocated by economic prices and/or markets, e.g., *full* cost pricing for water and sewage services or markets for irrigation water (AiA).

Further, some non-quantified aspects -- e.g., monopolistic water managers with asymmetric information advantage over regulators and customers -- can be (performance insurance).

Structure institutions to deliver the «right» high-powered or low-powered incentives (when worlds collide)

...see [kysq.org/pubs](http://kysq.org/pubs)

## In short...



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Good governance makes us happy, but we will only get it if we make the effort to watch our leaders and change outdated or unfair policies.

Expand



**Thanks!**

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